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REMARKS/ARGUMENTS

Reconsideration of this application is respectfully requested in view of the foregoing amendments and discussion presented herein.

1. **Restriction Requirement.**

The Examiner asserted that the application contains claims directed to patentably distinct species; that is, Group 1 containing Claims 1 and 22; Group 2 containing Claims 2-10, 21 and 23-32; Group 3 containing claims 11-20; and Group 4 containing Claims 33-43. Accordingly, election has been required.

Applicant confirms the election of Group II including claims 2-10, 21 and 23-32, as made in the telephone interview on June 19, 2006 and has canceled the remaining claims in this amendment.

2. **Rejection of Claims 2-7, 23-24 and 27-29 under 35 U.S.C. § 102(b).**

Claims 2-7, 23-24 and 27-29 were rejected under 35 U.S.C. § 102(b) as being anticipated by Levine (U.S. No. 5,477,038).

After carefully considering the grounds for rejection the Applicant responds as follows.

(a) **Claim 2.** Independent Claim 2, which is drawn to a method for facilitating payment transactions, has been amended to recite the aspects of the invention with greater particularity.

It will be readily appreciated that the system of Levine differs substantially from the invention recited in Applicant claims. The Levine system is directed to providing a card based travelers check, wherein a number of constraints and problems arise with regard to the use of that system for the purpose of the present invention. Appendix A is provided by the inventor for summarizing definitions, laws and processes governing aspects of prepaid cards. One reason that many of these problems and limitations from Levine do not arise in the claimed invention is that Applicant's system and method is configured around a trust account mechanism.

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Novel Trust Account Mechanism

In support of the rejection, Levine is said to teach accessing funds *"by a trustee and responsive to a monetary remittance from the cardholder (column 2, lines 47-67 through column 3, line 1)."*

However, Levine does not teach the use of a trust account, or a trustee, in the above referenced section or anywhere in the cited reference. The relied-upon section of Levine describes manufacturing of the cards and the process of distributing them to sales agents which sell a particular serial number that is then looked up by a remote computer which determines a location in the database to load with user information. Levine is built on a conventional prepaid card structure with a segmented account of the issuer accessed through a proprietary process performed at an ATM.

In contrast to Levine, the claims of the application, including Claim 2, are built on a trust account mechanism for containing the aggregate of the balances and configured for transaction execution over the existing payment infrastructure. This trust account core of the claimed invention provides numerous significant advantages over any conventional payment cards, including that of the Levine reference.

Claim 2 has been amended to bring out aspects of the trust account relationship with greater particularity. The step of generating a virtual account is described as being *"on behalf of a user, within a trust account configured for aggregating a plurality of virtual accounts under the control of a trustee"*. The claim goes on to describe the trust account as *"configured with an associated repository of capital sufficient to disburse funds by said trustee equivalent to the cumulative balances within the associated virtual accounts"*. It is the nature of the trust account that monies are held as an asset by the trustee which has a fiduciary obligation to disperse funds only at the direction of the trustor (not considering trust maintenance fees which may be a part of the trust agreement).

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A trust account by its nature is secure and federally insured. This is one reason why the instant application is referred to as "Ubiquitous Enablement of Electronic Currency", as the payment cards provide a true electronic currency form, with the trustee being obligated to disperse the associated monies to, or on behalf of, the cardholder (as described below).

As the nature of trust accounts was considered well known to those of ordinary skill in the art, the specification did not provide detailed background information on them in accordance with the tenets of MPEP 2164.01.

A patent need not teach, and preferably omits, what is well known in the art. *In re Buchner*, 929 F.2d 660, 661, 18 USPQ2d 1331, 1332 (Fed. Cir. 1991); *Hybritech, Inc. v. Monoclonal Antibodies, Inc.*, 802 F.2d 1367, 1384, 231 USPQ 81, 94 (Fed. Cir. 1986), *cert. denied*, 480 U.S. 947 (1987); and *Lindemann Maschinenfabrik GMBH v. American Hoist & Derrick Co.*, 730 F.2d 1452, 1463, 221 USPQ 481, 489 (Fed. Cir. 1984).

The following material is provided as an aid in understanding the use of a trust account within the present system. These sections are excerpted from Wikipedia the Free Encyclopedia, 2006, Search: Trust Law, URL:

http://en.wikipedia.org/wiki/Trust_law, site last modified 5 October 2006.

In common law legal systems, a **trust** is a relationship in which a person or entity (the *trustee*) holds legal title to certain property (the *trust property* or *trust corpus*), but is bound by a fiduciary duty to exercise that legal control for the benefit of one or more individuals or organizations (the *beneficiary*), who hold "beneficial" or "equitable" title. The trust is governed by the terms of the (usually) written trust agreement and local law. The entity (one or more individuals, a partnership, or a corporation) that creates the trust is called the settlor, and in the United States, the **trustor**, **grantor**, **donor**, or **creator**, as well.

Basic Principles

The trust has been called the most innovative contribution of English legal thinking to the law.[citation needed] Developed from the 11th century onwards, It plays an important role in all common law legal systems. Trusts developed out of the English law of equity which has no direct equivalent in civil law jurisdictions. However, since the use of the trust is so widespread, some civil law jurisdictions have incorporated trusts into their civil codes. Civil law systems also have analogous concepts like patrimony of affectation and

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the foundation that have similar independent patrimonies from their donors that trusts can have from their grantor.

A simple example of a trust which is common in real life is the situation where Joe Bloggs makes a will, including the clauses:

I appoint John Smith to be my executor.

I give my estate to my daughter Doris Bloggs if she attains 18.

Here, if Joe Bloggs dies while Doris Bloggs is still under 18, a trust comes into existence at that time, of which John Smith is the trustee and Doris Bloggs is the beneficiary. The Ownership of the trust's assets has become split:

The trustee has legal ownership. In our example, John Smith's name will go onto any title deeds, and he will be the signatory on any bank account.

The beneficiaries have equitable ownership. In our example, only Doris Bloggs has any right to enjoy the assets left by her deceased father. John Smith is not entitled to a penny from them. (In practice, of course, if John Smith is a professional trustee, there will certainly be another clause in the will which ensures that he is paid.) Notice, though, that Doris Bloggs is not entitled to this money outright - she only becomes entitled if she attains 18 - so her equitable ownership is not the same as outright ownership.

This dual title (legal versus equitable) is frequently called "split title." The "title split" of trust law may be generalized colloquially as follows: legal title involves control, management, and possession, while equitable (beneficial) title involves "benefit," "enjoyment," and "use."

Note from the above that there exists a fiduciary duty to the beneficiary who holds "beneficial" or "equitable" title on the asset. It will be clear to one of ordinary skill in the art that the monetary value of the payment card remains an equitable asset of the cardholder. It should be appreciated that with conventional prepaid payment cards (i.e., including the card of Levine) the card issuer (not the cardholder) owns the money remitted to them, with no assurance of funds being dispersed to, or on behalf of, the cardholder. If the issuer becomes insolvent then the prepaid card has no value. Appendix B discusses proposed FDIC legislation (first proposed in 2004) toward attempting to insure funds within stored value cards. From this discussion of the

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proposed legislation it can be understood that: (1) at least since 2004 the problem has been recognized, and (2) that no protection solution is presently available for these funds. It can be appreciated how this drawback of conventional payment cards would militate against their use as a store of value for any sizable monetary amount. The present invention, however, is well suited for storing substantial monetary value, an example is described in the specification on page 33, line 21 through page 34, line 7; wherein a person receives their wages within the VAP card of the present invention. In addition page 37, lines 3-6 describes using the VAP card for other large value storage: *"Card values set at the time of activation may be configured with arbitrarily large card values, subject to applicable regulations. For example, a card may be obtained with a virtual account balance of ten thousand dollars (\$10,000) to allow the cardholder to easily carry cash for use abroad, or for transfers to other parties."*

So it can be readily understood that significant value is provided by the structure of the present system, as it allows for the safe use of this form of payment card for large monetary assets. Therein the money of the beneficiary is protected despite the insolvency, bankruptcy, and so forth of the issuing institution.

The specification discusses the relationship of the bank or financial institution to the funds of the repository of capital underlying the virtual accounts within the trust. For example, the trustee of the account is described on page 20, lines 10-13: *"the trustee of the trust account is a bank or other financial institution that is appointed to administer the funds within the trust account."* Accordingly, the cardholder is the beneficiary and remains legally entitled to the right to disburse funds put into the trust account despite the insolvency of the bank or institution holding the funds. As discussed in the attached information from the inventor, Trust funds deposited under section 3(1)(2) of the FDIA, 12 U.S.C. 1813(1)(2) are defined as funds held by an insured depository institution in a fiduciary capacity.

A trust account is NEVER subject to bankruptcy of the trustee, and the bank controlling the trust is legally liable for all account balances. The transfer is performed

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concurrent with the authorization. "Trust funds" are defined by the industry as deposits under section 3(1)(2) of the FDIA, 12 U.S.C 1813(1)(2).

Merchant Chargeback Liability

According to the above discussion, the Levine system does not assure that the monetary value of the card remains accessible to the cardholder. The Levine system also provides no assurance that the merchant will be paid in response to completing a transaction, due to the liability and risk of chargebacks.

It will be helpful to understand certain aspects on the nature of the Levine teachings prior to proceeding. Levine is built on a conventional prepaid card structure with a segmented account of the card issuer accessed through a proprietary ATM protocol. Although Levine alludes to the use of Direct Deposit Accounts (DDAs) which are typically associated with a debit card, DDAs cannot legally comprise accounts from unnamed individuals. This condition could not be met by Levine which requires the sub-account to be looked up, for example referring to column 2, lines 59-67; and column 4, lines 47-55; wherein the process is described of looking up the BIN and account number for a given serial number.

The electronic travelers check (ETC) card of Levine is a prepaid card which acts as a front-end for, and relies totally on, the VisaNet network. A prepaid card transaction can be executed over the VisaNet network, if and only if, the POS terminal is a VisaNet terminal and that Visa terminal is Visa Interlink enabled (or its equivalent, if any). It will be noted that debit card transactions are signature based unless processed online via such a facility, while Levine is exclusively PIN based. Alternatively, the ATM can be provisioned with Visa Host-Based Stored Value infrastructure which is specifically designed to facilitate the processing of a prepaid card transaction, but presently facilitates only Visa Buxx, Visa Gift card, Visa TravelMoney and Visa Payroll card transactions. Neither Visa Interlink nor Visa Host-Based Stored Value protocols are disclosed by Levine. Additionally, effective November 30, 2004, Visa allowed issuers to permit cardholders who are dissatisfied with the delivery or quality of their purchases

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made with their Interlink cards to dispute the charges with their issuers for Interlink card transactions that are processed by Visa.

The liability for chargebacks within Levine contrasts to how the charges are irrevocably settled immediately in the system of the claimed invention. In addition, it should be appreciated that the system of the instant application does not require proprietary configurations of an ATM network and is instead configured for use over the existing transaction infrastructure.

As there exists a number of drawbacks to the Levine approach, it is not surprising that the approach of Levine has failed in the United States to fulfill a role as an electronic travelers check, and Visa has foregone the process described by Levine in deference to the use of the Visa TravelMoney Card which is a host-based stored-value system. A prepaid card instrument according to Levine could not be presented through VisaNet, or any other conventional network, at this time to execute payments or transfer transactions.

Returning to the discussion of merchant payment, it should be recognized that a proprietary ATM format is required by Levine or the conventional debit card (alluded to by Levine). An additional shortcoming of the Levine system is that even after authorization, there is no guarantee the merchant will get paid for the transaction. Transactions using the Levine system will be subject to chargebacks, wherein the merchant may not be paid for an executed transaction. The prepaid card of Levine is processed in the manner wherein the deduction from the account does not occur at the time of the transaction, but within a later batch transaction. In column 1, lines 37-41 Levine states: *"The immediate deduction is actually a same day or same night deduction, since the amount of the transaction is typically recorded, and then actually processed in batch mode at night with other transactions."* As a natural consequence of batch mode, the account can become overdrawn, and chargebacks can also arise wherein the account lacks assurances to both parties. These aspects are intrinsic problems with the structure of the Levine system and they lead to additional limitations

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of the Levine teachings. Levine does not describe how to overcome these situations, but teaches overcoming the problem of a lost card by imposing a daily limit of \$200 on withdrawals from a particular card (see column 1, lines 43-45), which would limit exposure to losses by merchants. However, it should be appreciated that the merchants would still be subject to risk, while using these monetary limits would not be in keeping with the tenets of the instant application which allows storing and accessing large cash values.

In contrast with these Levine teachings, Claim 2 of the instant application recites that executing the payment transaction involves "*immediately transferring*" a given portion of the balance. In addition, the transaction is executed "*without subjecting the merchant to a chargeback liability*". This is in keeping with a clear object of the invention as outlined on page 17, lines 21-23: "*Another object of the present invention is to provide a payment card that may be accepted as cash, wherein the merchant and acquiring institution do not incur a chargeback liability.*" In the claim the immediate transfer of funds is described "*as trustee releases a level of funds from the trust account in response to user directive, to render payment for executing said payment transaction*".

Accordingly, the instant application assures continued value to the cardholder while assuring payment to merchants. The claims recite elements of the invention which are not taught by the relied-upon reference, wherein the Applicant respectfully requests that the rejection of Claim 2, and the claims that depend therefrom, be withdrawn.

(b) Claim 23. Independent Claim 23 is drawn on a system for facilitating payment transactions and is written in a means-plus-function format. The arguments put forth against independent Claim 23 are the same as those used to support the rejection of independent Claim 2.

In a similar manner as Claim 2, Claim 23 describes a payment card structure built around a "*trust account*" mechanism and the execution of transactions

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"*immediately upon authorizing said payment transaction*". Claim 23 also describes that the trust account is controlled by a trustee in response to directives from the cardholder of each said virtual account.

The system of Levine does not teach the use of a trust account mechanism controlled by a trustee and it does not teach the immediate execution of transactions through the trustee when executing a payment transaction.

Therefore, as Claim 23 recites elements which are not taught by the relied-upon reference of Levine, the rejection of Claim 23 and the claims which depend therefrom should be withdrawn.

(c) Claims 3-7, 24 and 27-29. In view of the arguments and amendments presented for independent Claims 2 and 23, this group of dependent claims should be considered *a fortiori* allowable.

3. Rejection of Claims 8-10, 21, 25-26 and 30-32 under 35 U.S.C. § 103(a).

Claims 8-10, 21, 25-26 and 30-32 were rejected under 35 U.S.C. § 103(a) as being unpatentable over Levine as applied to claims 2 and 23 above, and further in view of Kolling et al. (U.S. Pat. No. 5,920,847).

After carefully considering the grounds for rejection the Applicant responds as follows.

Claim 21. A number of shortcomings arise in supporting the rejection of independent Claim 21 utilizing a combination of the Levine and Kolling references.

The rejection relies on combining the ability to increment and decrement an account from Kolling with the teachings of Levine put forth in the rejection against independent claims 2 and 23.

However, independent Claim 21 of the instant application describes a payment card system built around a trust account mechanism which is not taught by Levine, as described by the arguments put forth for preceding independent Claims 2 and 23. There are a number of additional shortcomings that arise from the rejection, the

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following being directed to a few of these shortcomings.

Not All Claim Limitations Taught or Suggested

Neither of the cited references (Levine or Kolling) provides any teaching, suggestion, or motivation for basing a payment card on a trust account structure. The only place an incentive for this is found is in the Applicant's own teachings.

2143.03 All Claim Limitations Must Be Taught or Suggested

To establish *prima facie* obviousness of a claimed invention, all the claim limitations must be taught or suggested by the prior art. *In re Royka*, 490 F.2d 981, 180 USPQ 580 (CCPA 1974). "All words in a claim must be considered in judging the patentability of that claim against the prior art." *In re Wilson*, 424 F.2d 1382, 1385, 165 USPQ 494, 496 (CCPA 1970). If an independent claim is nonobvious under 35 U.S.C. 103, then any claim depending therefrom is nonobvious. *In re Fine*, 837 F.2d 1071, 5 USPQ2d 1596 (Fed. Cir. 1988).

The use of a trust account provides a number of advantages as discussed in the specification. The advantages of using the trust account structure within the Applicant's payment card system have thus been put forth and should not be ignored in considering the patentability of the invention as a whole.

MPEP 716.02(f) Advantages Disclosed or Inherent

The totality of the record must be considered when determining whether a claimed invention would have been obvious to one of ordinary skill in the art at the time the invention was made. Therefore, evidence and arguments directed to advantages not disclosed in the specification cannot be disregarded. *In re Chu*, 66 F.3d 292, 298-99, 36 USPQ2d 1089, 1094-95 (Fed. Cir. 1995) (Although the purported advantage of placement of a selective catalytic reduction catalyst in the bag retainer of an apparatus for controlling emissions was not disclosed in the specification, evidence and arguments rebutting the conclusion that such placement was a matter of "design choice" should have been considered as part of the totality of the record. "We have found no cases supporting the position that a patent applicant's evidence or arguments traversing a § 103 rejection must be contained within the specification. There is no logical support for such a proposition as well, given that obviousness is determined by the totality of the record including, in some instances most significantly, the evidence and arguments proffered during the give-and-take of *ex parte* patent prosecution." 66 F.3d at 299, 36 USPQ2d at 1095.). See also *In re Zenitz*, 333 F.2d 924, 928, 142 USPQ 158, 161 (CCPA 1964) (evidence that claimed compound minimized

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side effects of hypotensive activity must be considered because this undisclosed property would inherently flow from disclosed use as tranquilizer); *Ex parte Sasajima*, 212 USPQ 103, 104 - 05 (Bd. App. 1981) (evidence relating to initially undisclosed relative toxicity of claimed pharmaceutical compound must be considered).

In addition, the desirability of basing a payment card on a trust account is nowhere taught or suggested by the Levine reference. It should be noted that the basis of the Levine reference is a payment card incorporating a travelers check structure. The desirability of modifying the reference is not found in the cited references.

The Federal Circuit states that "[t]he mere fact that the prior art may be modified in the manner suggested by the Examiner does not make the modification obvious unless the prior art suggested the desirability of the modification." In re Fitch, 972 F.2d 1260, 1266 n.14, 23 USPQ2d 1780, 1783-84 n.14 (Fed. Cir. 1992), citing In re Gordon, 733 F.2d 900, 902, 221 USPQ 1125, 1127 (Fed. Cir. Appeal No. 97-0315 Application 08/336,181 -6-1984).

In addition to being based on a trust account mechanism, it should be noted that amended Claim 21 describes aspects of the trust account with greater particularity. In addition, the claim describes settling transactions in response to the trustee releasing a level of funds from the trust account in response to cardholder directives. Furthermore, the claim also describes how the transaction is immediately settled from the trust account in response to processing said transaction, wherein no chargeback liability is incurred, such as to a merchant.

Different Objects and Operating Principles

Levine teaches a system of "*electronic travelers cheque*" (ETC) (col. 2, line 9) in a card form and configured to operate as a pooled prepaid card. The sub-divided account used within Levine is clearly not a trust account, but instead a conventional account of the entity which is selling the payment cards. There is no trustee of the account (as that term is used conventionally and within the specification of the application) and its associated fiduciary obligations to the cardholder as beneficiary.

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It should be noted that the electronic travelers check metaphor of Levine is subject to a number of regulatory constraints complicating deployment of the system. For example, Title XXXIV-A of the Uniform Commercial Code (U.S), Negotiable instruments, Section 382-A:3-104 sets forth a number of requirements for a "Traveler's Check" form of instrument, including: *"requires, as a condition to payment, a countersignature by a person whose specimen signature appears on the instrument"*. Numerous additional financial restrictions exist, such as put forth by the National Automated Clearing House Association (NACHA), which maintains that the presenter of a travelers check is not the owner of the account on which the instrument is drawn, and thus cannot properly authorize the instrument's conversion to an ACH debit.

Another large problem typifying the system of Levine is that the cards fall into the category of prepaid cards. This is not just a grammatical or structural distinction, but even a legal one. The cards of Levine are not issued, but must be sold through the agent. The monies from the cardholder become the property of the card issuer. The money in the pool is NOT federally (i.e., FDIC) insured for the cardholder, and the cardholder thereby has no guarantee of sustained value. Consequently, the value of the prepaid card is not secure, as it is owned by the card issuing institution and its value depends on the institution.

Those in the industry recognize that numerous persons have lost the value of prepaid cards when a seller or institution declares bankruptcy, or otherwise is unable to meet its obligations. In fact prepaid cards are not currently the subject of ANY federal consumer protection laws or regulations in the United States. Regulation Z which protects credit card consumers does not apply to prepaid cards, and Regulation E which protects debit card users and ACH transfers, similarly does not apply to the prepaid cards as discussed by Levine. The underlying monetary account of Levine has no protection, it is a conventional prepaid card based on a segmented unsecured account. Therefore, such cards are not a secure means of retaining value.

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In addition one working with trust accounts will recognize that they are not subject to the same escheat laws as are accounts to which conventional prepaid cards and debit cards are subject. For many years, all trusts had a limited life span, with most states using a rule descended from feudal England which required all interests to vest no later than the greater of 90 years or "lives in being plus 21 years," which generally allowed a trust to continue for approximately 90 to 120 years before the trustee would have to distribute the trust assets to the beneficiaries. This is the common law rule against perpetuities. To simplify the rules concerning the duration of a trust, Delaware repealed its common law rule against perpetuities in 1986 and replaced it with a simple 110-year limitation. Thus, a trust could last 110 years even if its terms violated the common law rule against perpetuities. In 1995, Delaware further liberalized its laws by abolishing the 110-year limitation for all trust property except real estate. Therefore, under that legislation, a trust holding personal property can last indefinitely. Today, seventeen states and Washington, D.C. have laws allowing trusts to continue perpetually. Accordingly, in states without laws against perpetuity, the trust account remains perpetual.

In any case the life of a trust exceeds the dormancy period associated with escheat laws which are typically in the range of 1-7 years for most states. According to Judith Rinearson, chief counsel to American Express' electronic stored-value business, citing: "Escheatment Issues Could Impact Stored-Value Cards," Card Technology News, March 7, 1997: "The time period that must elapse before the property is subject to escheatment varies, depending on the state and the property involved (e.g., 15 years for travelers' checks and three to five years for gift certificates). For general unclaimed funds, 35 states have a five-year period; seven states have a seven-year period; eight states have a three-year period; and New York has just a two-year period." The perpetuity or long-life span of a trust provides the advantage that monies of a trust account are not turned over, or not turned over so readily, to the local jurisdiction in response to a period of account inactivity.

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Accordingly, the combination does not teach, suggest, or provide motivation for the payment card of Claim 21 which involves the use of a trustee controlling a trust account, and settling transactions immediately without chargebacks.

Therefore, Applicant asserts that Claim 21 is not obvious in view of the cited references and respectfully requests that the rejection of Claim 21 and the claims which depend therefrom should be withdrawn.

4. Cancellation of Claims 1, 10-20, 22, and 33-43.

Claims 1, 11-20, 22, and 33-43. In response to the restriction requirement, Claims 1, 11-20, 22, and 33-43 have been canceled.

Claim 10. The material of dependent Claim 10 has been incorporated into Claim 2, and Claim 10 has been canceled.

5. Amendment of Claims 2-3, 5, 9, 21, 23-27, 29 and 31-32.

Claims 2, 21 and 23. Independent Claims 2, 21 and 23 have been amended to recite a number of aspects with increased particularity, support for which is found in the specification as outlined below.

A virtual account is created on behalf of a user, with the virtual account within a trust account configured for aggregating a plurality of virtual accounts. Support is found in the original claims as well as throughout the specification, including page 18, lines 22-29; page 15, lines 4-9; page 19, line 18 through page 20, line 7; page 20 line 9-12; and so forth.

The trust account being configured with an associated repository of capital sufficient to disburse funds equivalent to the cumulative balances within the associated virtual accounts is taught in the specification, as well as within original Claim 21 and 26.

Issuing the payment card encoded with virtual account number is supported throughout the specification, including page 20, lines 7-14; and so forth.

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The "*immediately transferring*" of a portion of the balance of a virtual account in response to release by the trustee is described in the specification, such as at page 16, lines 24-28; page 25, lines 25-28; page 26, lines 3-10; page 27, lines 17-18; page 36, lines 9-15; and elsewhere. Support for the aspect in which there is no chargeback liability is in the specification, such as at page 17, lines 21-23; and page 23, lines 6-12.

Claim 3. Dependent Claim 3 is amended as the issuance of the payment card is now described in the base claim, wherein Claim 3 has been amended to recite that the activation of the card is performed according to this dependent claim as part of the issuing process of Claim 2.

Claim 5 and 29. Dependent Claims 5 and 29 have been amended to replace the phrase "*as the means of payment when the card is tendered to a merchant*" with "*as the means of payment to a merchant*". The "*tendered*" phrase portion has been removed to eliminate the possibility of this being construed too narrowly as requiring physical submission of the card to a merchant. Support for this change is found throughout the specification, including: page 17, lines 3-5; page 29, lines 18-22; and so forth.

Claim 9. Dependent Claim 9 has been amended to recite use of the payment card "*through the existing payment card infrastructure*" which seems to increase clarity over the phrasing "*same or similar manner as that used for a debit card*", as was previously recited. Support is found in the specification, such as at page 29, lines 5-9.

Claim 24. The material of dependent Claim 24 was incorporated into base Claim 23. Claim 24 has been amended to recite the holding of the virtual account anonymously. Support for this anonymous virtual account aspect is found in the specification, including page 30 lines 14-18.

Claim 25. Dependent Claim 25, which describes the retaining of historical information, has been amended to recite more details of the historical aspect within a means context. Support for this history mechanism is found in the original Claim 25 as well as throughout the specification, including page 20, lines 16-20, and so forth.

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Claim 26. The material of original Claim 26 was incorporated into base Claim 23, and dependent Claim 26 has been amended to describe the ability to recharge the virtual account within the trust account. Support is found in original Claim 8, as well as throughout the specification of the instant application, such as at page 1, lines 25-28.

Claim 27. The material of original Claim 27 was incorporated into base Claim 23, and dependent Claim 27 was amended to depend from Claim 26 and describe specific means for incrementing the virtual account balance. Support is found throughout the specification, including page 33, lines 11-20.

Claim 31. Dependent Claim 31 was amended in a similar manner as Claim 9 to recite the phrase "*through the existing payment card infrastructure*" instead of describing "*in the same or similar manner as a debit card transaction*", to reduce any possible source of confusion within the claim.

Claim 32. Dependent Claim 32 has been amended to replace the phrase "issuing bank" with the phrase "*issuing bank, or institution,*" as the specification makes it clear that the trust account payment card can be issued by banks or institutions. Support is found in the specification, including page 4, lines 11-14; page 6, lines 3-6.

6. Addition of Claims 44-54.

Claim 44. Dependent Claim 44 recites the virtual account being held anonymously by said user as cardholder. Support for this anonymous virtual account aspect is found in the specification, including page 30 lines 14-18.

Although Claim 44 should be considered *a fortiori* allowable in view of the discussion of the patentability of its base claim, it provides additional grounds for patentability.

It should be noted that Levine requires name and identification as it models a travelers check, and identification is required for cashing a travelers check. See column

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1, lines 61-64: *"Travelers cheques are desirable as compared to currency because of the signature authorization required..."*.

The card of Levine cannot be used anonymously, the summary of Levine teaches that the information for each card contains *"blank fields for the customer data (name, address, etc.)..."* (see also page 11, lines 31-32). This also fits with a travelers check in that the person acquiring the travelers check must be identified. The system of Levine also follows the paradigm of a paper travelers check in that the value is only set through the use of an agent processing the card for an institution. Actually in Levine a neutral third party (VISA) performs the processing on behalf of the issuer. This mechanism fulfills a legal requirement for such a prepaid card which is "issued" to the sales agent, and "sold" to the card holder. A prepaid card such as described by Levine can not be legally "issued" to the cardholder. In addition, the user can not recharge the card because it is purchased as a fixed value card, it is not a deposit, nor is any mechanism disclosed by Levine toward recharging the cards.

Also in Levine, see page 3, lines 17-25: *"The ETC processor establishes a zero balance database including the card numbers, but with blank fields for the customer data (name, address, etc.) and the value of the card. The cards are provided to a bank or other sales agent. When a customer purchases a card, the sales agent uses local software to remotely transmit to the central database the card number (or a serial number) along with the customer data and the amount purchased."*

One of ordinary skill in the art of financial instruments will also appreciate that since a conventional prepaid card can be subject to chargebacks that the accounts cannot be anonymous as the user could not then be tracked for the balance. In addition, a travelers check, by both definition and current law, requires a signature (see page 5 of Appendix A).

Claim 44 describes holding the virtual accounts anonymously. Support for this aspect is found in the specification, including page 30, lines 14-18; page 32, lines 1-7; and so forth.

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Claims 45-46. Dependent Claim 45 recites that the payment transactions of Claim 2 can be directed to a merchant, or as a transfer of funds into another virtual account within the trust account. Claim 46 extends this distinction to describe transferring the funds without the need to receive an authorization from the receiver prior to fund transference. The aspect which enables the user as cardholder to transfer any portion of a balance from their virtual account to the virtual account of another user is described in original claims 6, 8, 16, 18 and 21. In addition, support for transferring balance portions to other virtual accounts is found throughout the specification, including page 16, lines 20-22; page 23, lines 5-7; page 28, lines 9-12; page 37, lines 4-6; and so forth.

Although Claims 45-46 should be considered *a fortiori* allowable in view of the discussion of the patentability of its base claim, these claims provide additional grounds for patentability.

Transferring to other virtual accounts is not taught by the cited references and neither is it obvious in view of the cited references. Levine does not teach transferring portions of the value from the travelers check card to other travelers check cards, and no mechanism is described in support thereof. Levine does not even teach the use of mechanism for recharging the card, which would be a necessary aspect of transferring any balances. The Kolling reference is not even directed at payment cards, but at performing on-line banking. Without using hindsight based on the instant application, there is thus no teaching, motivation or incentive for attempting to structure a payment card device according these claims.

Therefore, these aspects of the invention are not obvious with respect to the recited references.

Claim 47. Dependent Claim 47 describes recharging of the virtual account within the associated trust with the payment card of the instant application. Levine does not teach a rechargeable aspect. It will be appreciated that Levine is specific to a disposable card, as seen in column 2, lines 19-21: "*The card is disposable when the*

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account is depleted, with a new card and account required for a new amount of cash."

Claim 47 should be considered *a fortiori* allowable in view of the discussion of the patentability of its base claim.

Claim 48-54. Dependent Claims 48-54 contain material of Claims 3-9 directed at base Claim 2, which have been added herein to now depend from independent Claim 21.

7. Amendments Made Without Prejudice or Estoppel.

Notwithstanding the amendments made and accompanying traversing remarks provided above, Applicant does not acquiesce in the original ground for rejection with respect to the original form of these claims. These amendments have been made without any prejudice, waiver, or estoppel, and without forfeiture or dedication to the public, with respect to the original subject matter of the claims as originally filed or in their form immediately preceding these amendments. Applicant reserves the right to pursue the original scope of these claims in the future, such as through continuation practice, for example.

8. No Additional Claim Fees.

Although claims have been added to the case, the number of claims originally filed still exceeds the number of claims presently pending in the case, wherein no additional claim fees are due.

9. Conclusion.

Based on the foregoing, Applicant respectfully requests that the various grounds for rejection in the Office Action be reconsidered and withdrawn with respect to the presently amended form of the claims, and that a Notice of Allowance be issued for the present application to pass to issuance.

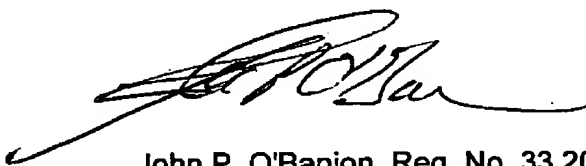
In the event any further matters remain at issue with respect to the present

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application, Applicants respectfully request that the Examiner please contact the undersigned below at the telephone number indicated in order to discuss such matter prior to the next action on the merits of this application.

Date: 10/16/06

Respectfully submitted,



John P. O'Banion, Reg. No. 33,201
Rodger H. Rast, Reg. No. 45,853
O'BANION & RITCHEY LLP
400 Capitol Mall, Suite 1550
Sacramento, CA 95814
(916) 498-1010

The Laws and Processes That Govern the Domain

The domain of electronic payment systems is highly regulated; the conventions and processes associated with the industry are comprehensive, complex and well known to those familiar with the art. Some of the most obvious issues that relate to the present invention and the Levine patent are excerpted and paraphrased hereinafter for convenience and offer some insight into the significant differences between the two processes and the environments within which each must function.

The current status of stored value cards relative to Regulation E can be summarized as follows:

In 1996, the Federal Reserve Board proposed amendments to Reg E and the Reg E commentary to clarify how, and under what circumstances, Reg E would apply to stored value cards. That proposal was never finalized. Instead, the Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA) was passed and it required the FRB to study and report to Congress on the impact of application of the EFTA to stored value cards, which the FRB did in 1997. In most cases, a stored value card does not access a consumer's account and thus would not arguably come within the purview of Regulation E. In order to allow the technology to evolve without overly burdensome regulation, the FRB has taken little action to date (http://www.bankersonline.com/ebanking/gurus_eb031102a.html).

Those familiar with the art are aware of the following:

Definition of Terms:

Deposit and Demand Deposit Account (DDA)

Pursuant to General Counsel Opinion No. 8 (<http://www.fdic.gov/regulations/laws/rules/5500-500.html>), of the FDIC, typically, stored value cards are touted as substitutes for cash. Technically, however, they are not cash, and they do not have the finality of cash. Moreover, what is actually stored on stored value cards is information that, through the use of programmed terminals, advises a prospective payee that rights to a sum of money can be transferred to the payee, who in turn can exercise such right and be paid. While this opinion addresses stored value cards, the Legal Division believes that in general the principles discussed herein would apply equally to stored value computer network payment products.

The term "deposit" means, in part, funds held by such bank or savings association, whether held in the trust department or held or deposited in any other department of such bank or savings association. Trust funds are deposits under section 3(l)(2) of the FDIA, 12 U.S.C. 1813(l)(2) (i.e. Trust funds as defined in this Act received or held by such bank or savings association, whether held in the trust department or held or deposited in any other department of such bank or savings association). For purposes of the FDIA, trust funds are funds held by an insured depository institution in a fiduciary capacity, including funds held as trustee, executor, administrator, guardian or agent, 12 U.S.C. 1813(p). The FDIC staff is not aware of stored value card systems in which funds are held by an institution in a fiduciary capacity. Stored value cards are not negotiable instruments. A stored value card is not in writing, not signed by the maker, and does not contain an unconditional promise to pay a sum certain in money and no other promise, order, obligation or power. With respect to the other provisions of section 3(l) of the FDIA, 12 U.S.C. 1813(l), the FDIC staff is not aware of stored value card systems in which funds will be held as trust funds. The funds underlying stored value cards would not be deposits under section 3(l)(2) of the FDIA, 12 U.S.C. 1813(l)(2). While stored value cards have certain similarities to cashier's checks and money orders, they are not drafts drawn on the bank, nor are they negotiable instruments. Consequently, they cannot be considered deposits under section 3(l)(4) of the FDIA, 12 U.S.C. 1813(l)(4).

The four categories specified by the FDIC General Counsel that currently define stored value cards are:

- Bank Primary-Customer Account Systems — funds remain in the customer's bank account until the electronic value is transferred to a merchant or other payee. Funds underlying Bank Primary-Customer Account Systems are "deposits" of the customer
- Bank Primary-Reserve Systems — when value is downloaded onto the customer's card, funds are transferred from the customer's account to a reserve or general liability account held at the institution to pay merchants and other payees. Funds underlying Bank Primary-Reserve Systems are not deposits under the statutory definition.
- Bank Secondary-Advance Systems — the issuer of the card is a third party, which provides electronic value to banks to make available to their customers; the customers then pay the third party for the stored value out of their bank accounts. Funds underlying Bank Secondary-Advance Systems for the (presumably brief) period prior to their transfer to the issuer are "deposits" of the issuer.
- Bank Secondary-Pre-Acquisition Systems — the issuer of the card is a third party; banks pay the third party for the electronic value and subsequently resell that value to bank customers. Funds underlying Bank Secondary-Pre-Acquisition Systems are not deposits under the statutory definition.

Former FDIC Chairman Andrew C. Hove, Jr. has stated that the agency has decided not to propose regulations or seek legislative action to define stored-value cards as "deposits" for purposes of insurance coverage. The agency will continue to rely on guidance provided in General Counsel Opinion No. 8, which clarified conditions for stored-value cards to qualify for FDIC federal deposit insurance coverage. (<http://www.fdic.gov/news/news/press/1997/pr9744.html>) In the General Counsel opinion letter, published in the Federal Register on August 2, 1996, the FDIC concluded that in most cases stored-value cards are not protected by deposit insurance because the issuing institution would typically maintain a single pooled account to hold the funds represented by all their customers' stored-value cards. However, a bank customer's balance on a stored-value card would be covered by deposit insurance if the funds used to pay for goods and services with the card remain in the customer's account at the bank until the value is transferred to the merchant.

The FRB, pursuant to 12 U.S.C. 248(a), 248(c), 371a, 461, 601, 611, and 3105, provides that (excerpted for brevity):

(a)(1) "Deposit" means:

(i) The unpaid balance of money or its equivalent received or held by a depository institution in the usual course of business and for which it has given or is obligated to give credit, either conditionally or unconditionally, to an account, including interest credited, or which is evidenced by an instrument on which the depository institution is primarily liable;

(b)(1) "Demand deposit" means a deposit that is payable on demand, or a deposit issued with an original maturity or required notice period of less than seven days, or a deposit representing funds for which the depository institution does not reserve the right to require at least seven days' written notice of an intended withdrawal. Demand deposits may be in the form of:

(i) Checking accounts

(ii) Certified, cashier's and officer's checks;

(iii) Traveler's checks and money orders that are primary obligations of the issuing institution;

(2) The term *demand deposit* also means deposits or accounts on which the depository institution has reserved the right to require at least seven days' written notice prior to withdrawal or transfer of any funds in the account and from which the depositor is authorized to make withdrawals or transfers in excess of the withdrawal or transfer limitations specified in § 204.2(d)(2) for such an account and the account is not a NOW account, or an ATS account or other account that meets the criteria specified in either § 204.2(b)(3)(ii) or (iii) below.

(3) *Demand deposit* does not include

(i) Any account that is a time deposit or a savings deposit under this part;

(ii) Any deposit or account on which the depository institution has reserved the right to require at least seven days' written notice prior to withdrawal or transfer of any funds in the account and either--

(A) Is subject to check, draft, negotiable order of withdrawal, share draft, or similar item, such as an account authorized by "NOW Account" and a savings deposit described in § 204.2(d)(2), provided that the depositor is eligible to hold a NOW account; or

(B) From which the depositor is authorized to make transfers by preauthorized transfer or telephonic (including data transmission) agreement, order or instruction to another account or to a third party, provided that the depositor is eligible to hold a NOW account

The Office of the Comptroller of the Currency (OCC 96-48 Subject: Stored Value Card Systems Description: Information for Bankers and Examiners (<http://www.occ.treas.gov/ftp/bulletin/96-48.txt>) has found that the term *stored value card* typically refers to a card either with a magnetic stripe or with a computer chip that is charged with a fixed amount of economic claims or value that can be "spent" or transferred to individuals and/or merchants in a manner that is similar to spending paper money or coins. *Electronic cash* refers to stored value represented by a digital computer code that consumers use for payments processed through a computerized financial network. Although debit transactions also can be processed electronically, *electronic debit transactions* should not be confused with *true electronic cash transactions*. The distinction between stored value and debit transactions is significant because, although similar in some respects, they can present different regulatory and supervisory issues. A debit card is used to access an account, in order to withdraw or transfer funds from or to existing accounts. National banks may perform or have performed for them one or more of the functions in stored value card systems, each with a specific structure and level of risk. In most stored value card systems, transactions will be processed at the point of sale by an electronic device without further authorization. If the distributing agent bank fails to inform the purchaser (i.e., consumer) that it is acting as the agent of the issuer, a consumer might seek to hold the agent bank obligated on the electronic cash under a legal theory which imputes the liability of a principal to an agent that has caused others to reasonably believe that the supposed agent was acting as a

principal. Banks that authorize the exchange of electronic cash for goods and services are exposed to transaction risk. In all open stored value systems, holders of electronic cash will be able to convert electronic cash to currency or funds added to a bank deposit account. Clearing and settling a payment transaction requires transmitting both information and funds through a valid payment systems network. Banks involved in clearing and settlement may be continuing a role they undertook as redeemer for their customers or, alternatively, they may accept that role on behalf of other banks and act as an intermediary in the process through which the electronic cash is presented to the issuer for payment. Clearing and settling banks may be exposed to transaction, credit, liquidity and foreign exchange risk.

Debit Card — A debit card transaction involves the purchase of a good or service. Absent the generalization of the term for marketing purposes, the term is defined by the Board of Governors of the Federal Reserve System (FRB) as a card used at a point-of-sale (POS) terminal that enables a consumer to have funds directly debited from his or her bank Demand Deposit Account (usually a checking account). The FRB further limits the use of the term to a card that accesses a consumer account that is subject to the Electronic Fund Transfer Act and categorizes the term by the network on which related transactions are executed, either Online or Offline.

- Online transactions are effected and settled in real time, usually over a closed communications network, and rely on a PIN number for authentication by the issuing bank, or its processor.
- Offline transactions are effected and settled through an ACH credit card network, over a period of time, and rely on a signature for authentication by the issuing bank, or its processor.
- The primary purpose of a debit card is to electronically access funds maintained in a DDA, although some financial institutions may enable access to Negotiable Orders of Withdrawal (NOW) accounts which are not demand deposits but, rather, a class of savings deposits. They resemble checking accounts, which are demand deposits, in that they may be accessed by negotiable or transferable instruments (12 U.S.C. e 1832(a)). Unlike demand deposits, however, depository institutions may pay interest on NOW accounts by virtue of the fact that the depository institution has reserved the right to require at least seven days written notice prior to withdrawal. NOW accounts are marketed as interest-bearing checking accounts and funds are made available for withdrawal to depositors without delay. Federal Reserve Board Regulation CC, governing availability of funds, defines "account" to include both DDAs and NOW accounts (12 C.F.R. e 229.2(a)). The regulations require banks to make funds deposited in both types of accounts available for withdrawal on the same schedule (12 C.F.R. e 229.10).
- In a debit card transaction, participants are the consumer, the issuing bank, the merchant and the merchant's bank
- Online transactions are effected over an EFT network, a telecommunications and payments infrastructure linking consumers, ATMs, merchants and banks. In practice, a subset of EFT networks process Online POS transactions. Visa and MasterCard operate EFT networks. Each uses its own physical infrastructure to run ATM and Online POS transactions. Visa's Interlink and MasterCard's Maestro are Online POS networks.
- Offline transactions are effected over credit card networks, a telecommunications/payments infrastructure linking consumers, merchants and banks. The Visa network is Visa Check Card. The MasterCard network is MasterMoney. The physical components of the Offline debit network consist of POS terminals, telecommunication connections, apparatus that route transaction information to appropriate parties and computers that store deposit and transaction information. Information necessary for the authorization of an Offline debit transaction as well as information for processing the payment follow the same infrastructure routes as for credit card transactions.
- Online debit allows the cardholder to obtain cash back at the point of sale, while Offline debit does not.
- There are four categories of Online debit card transactions:
 - Native transactions are not routed through any network switch. In the simplest case, which is called an "acquirer on-us" transaction, a cardholder uses a debit terminal driven by the card issuer's processor. Because the entire transaction is routed only through the issuing bank's systems, there is no need to involve a network switch. A variation is where the acquiring bank and the card-issuing bank are different institutions, but use the same processor for routing transactions. Such transactions are called "processor on-us" transactions.
 - Network on-us transactions are routed through only one network switch. The switch can be either a regional network's or a national network's. Typically a network on-us transaction is initiated by a cardholder of one member institution at a POS debit terminal served by another member institution.
 - Reciprocal transactions occur when the cardholder makes a transaction at a POS debit terminal served by an acquirer other than the card-issuing bank; and the card issuer and acquirer use different regional networks, but the networks have a reciprocal sharing agreement. A reciprocity agreement between regional networks is an arrangement whereby the two networks agree to pass information to one another in transactions involving members of each network. As such, typically two switches are necessary to complete the transaction.

- National bridge transactions occur when the cardholder makes a transaction at a POS debit terminal served by an acquirer other than the card-issuing bank; and the card issuer and acquirer use different regional networks, but the networks do not have a reciprocal sharing agreement. In this case the card issuer and acquirer must belong to the same national network (Interlink or Maestro), and regional networks serve as gateways to the national network. The transaction involves three switches, one from the initiating regional network, one from the national network, and one from the other regional network
 - Offline debit card transactions — (Visa Check Card and MasterCard MasterMoney) are run over the Visa and MasterCard credit card networks and, hence, are processed differently from online debit transactions.
 - There are two manners of settlement: direct settlement and processor-level settlement.
 - For direct settlement, the network's clearing bank originates ACH to each member financial institution.
 - For processor-level settlement, the network's clearing bank originates ACH to processors, instead of originating ACH to each member who uses the processor.
- After the settlement between the network and the processor is completed, the processor or its clearing bank originates ACH to its customer financial institutions.

ATM Card — An ATM transaction typically involves withdrawing cash from an ATM machine.

- An ATM card is typically a dual ATM/debit card that can be used for both ATM and debit card transactions.
- Many ATM/debit cards offer the consumer both types of debit card transactions, Online and Offline.
- In an ATM transaction, users are the consumer, the card-issuing bank and the ATM owner.
- ATM transactions are executed over EFT networks. EFT networks are the telecommunications and payments infrastructure linking consumers, ATMs, merchants and banks. There are two types of EFT transactions. The first are ATM transactions. The second are Online debit transactions at POS terminals. EFT networks can be used for either ATM transactions or Online POS debit card payments or both. In practice, most EFT networks process ATM transactions, and a subset of these also processes POS transactions
- Visa and MasterCard operate EFT networks. Each uses its own physical infrastructure to run ATM transactions. Visa's Plus and MasterCard's Cirrus are ATM networks.
- There are four categories of ATM transactions:
 - Native transactions are not routed through any network switch. In the simplest case, which is called an "owner's on-us" transaction, a cardholder uses an ATM owned by his or her bank. Because the entire transaction is routed only through the issuing bank's systems, there is no need to involve a network switch. A variation is where the cardholder uses an ATM that does not belong to his or her bank but the card issuing bank and the ATM owner use the same processor. Some networks allow the processor to route transactions among its clients without involving the network switch, even when the ATM owner and the card issuer of the transaction are different institutions. Such transactions are called "processor's on-us" transactions.
 - Network on-us transactions are routed through only one network switch. The switch can be either a regional network's or a national network's. Typically a network on-us transaction is initiated by a cardholder of one member institution at an ATM of another member institution.
 - Reciprocal transactions occur when the cardholder uses an ATM of another institution and the card issuer and ATM owners use different regional networks, but the networks have a reciprocal-sharing agreement. A reciprocity agreement between regional networks is an arrangement whereby the two networks agree to pass information to one another in transactions involving members of each network. Typically, two network switches are necessary to complete the transaction.
 - National bridge transactions occur when the cardholder uses an ATM of another institution and the card issuer and ATM owners use different regional networks but the networks do not have a reciprocal sharing agreement. In this case the card issuer and ATM owner must belong to the same national network (Cirrus or Plus) and the regional networks serve as gateways to the national network. The transaction involves three switches, one from the initiating regional network, one from the national network, and one from the other regional network.
- There are two manners of settlement: direct settlement and processor-level settlement.
 - For direct settlement, the network's clearing bank originates ACH to each member financial institution.
 - For processor-level settlement, the network's clearing bank originates ACH to processors, instead of originating ACH to each member who uses the processor.

After the settlement between the network and the processor is completed, the processor or its clearing bank originates ACH to its customer financial institutions.

Traveler's Check — a preprinted, fixed-amount check designed to allow the person signing it to make an unconditional payment to someone else as a result of having paid the issuer (usually a bank) for that privilege. Traveler's checks do not expire, though in certain cases they may be subject to state escheat regulations. The legal terms for the parties to a traveler's check are the **obligor** or **issuer**, the entity that produces it; the **agent**, the bank or other entity that sells it; the **purchaser**, the natural person who buys it; and, the **payee**, the entity to whom the purchaser writes the check. For purposes of clearance, the obligor is both **maker** and **drawee**.

A Traveler's Check is a Negotiable Instrument as defined under TITLE XXXIV-A of the Uniform Commercial Code, Negotiable Instruments, Section 382-A:3-104, which provides that:

- (a) Except as provided in subsections (c) and (d), "negotiable instrument" means an unconditional promise or order to pay a fixed amount of money, with or without interest or other charges described in the promise or order, if it:
 - (1) is payable to bearer or to order at the time it is issued or first comes into possession of a holder;
 - (2) is payable on demand or at a definite time; and
 - (3) does not state any other undertaking or instruction by the person promising or ordering payment to do any act in addition to the payment of money, but the promise or order may contain
 - (i) an undertaking or power to give, maintain, or protect collateral to secure payment,
 - (ii) an authorization or power to the holder to confess judgment or realize on or dispose of collateral, or
 - (iii) a waiver of the benefit of any law intended for the advantage or protection of an obligor.
- (b) "Instrument" means a negotiable instrument.
- (i) "Traveler's check" means an instrument that:
 - (i) is payable on demand,
 - (ii) is drawn on or payable at or through a bank,
 - (iii) is designated by the term "traveler's check" or by a substantially similar term, and
 - (iv) requires, as a condition to payment, a countersignature by a person whose specimen signature appears on the instrument.

The American Banker's Association, pursuant to the Routing Number Policy of the Routing Number Administrative Board, requires traveler's checks to have Traveler's Check Identifiers - special purpose routing numbers intended for use on paper items issued by payors of traveler's checks. A Traveler's Check Identifier may be used in an electronic check file, but cannot be used for wire transfers, ACH or other electronic payments. Traveler's checks must be denominated in whole dollar amounts and must employ an algorithm in the MICR line "on-us" field which allows for the verification of the amount of the item. Items bearing traveler's check identifiers must be payable in a Federal Reserve city. Regarding the electrification of payment instruments, the National Automated Clearing House Association (NACHA), maintains that the presenter of a traveler's check is not the owner of the account on which the instrument is drawn, and thus cannot properly authorize the instrument's conversion to an ACH debit. This finding is in contrast to the electrification of payment instruments drawn against a Demand Deposit Account and/or a NOW account, wherein the presenter of the instrument is in fact the owner of the account and has the absolute right to authorize transactions against it.

Electronic Travelers Check — As defined by the Board of Governors of the Federal Reserve System in their *Report to the Congress on the Application of the Electronic Fund Transfer Act to Electronic Stored-Value Products*, March, 1997, a travelers check is a sight draft for a fixed amount paid in advance and signed twice by the purchaser, once when ordering the draft and once when cashing it. Travelers checks are payable by the issuing company and insured against loss or theft. There is no generally accepted definition of an "electronic travelers check." This study defines "electronic travelers check" as a product that is marketed as having features similar to those of the paper travelers check, such as immediate replacement by the issuer when the check is lost or stolen. [Levine was issued on December 19, 1995]

Prepaid and Stored Value Cards — The Federal Reserve Bank defines Prepaid Cards, sometimes referred to as a Stored-Value Card, to include travel cards as replacing traveler's checks. Prepaid cards are not currently the subject of any federal consumer protection laws or regulations. Regulation Z, which protects credit card consumers, does not apply to prepaid cards because prepaid card users are not being extended credit. Regulation E, which protects users of debit cards and ACH transfers, does not extend to prepaid cards because the account associated with such cards falls outside of the definition of "consumer asset account" — the type of account the statute was designed to protect.; (Regulation E, 12 C.F.R. § 205.2 (2004), defines an account covered by the regulation as "a demand deposit (checking), savings, or other consumer asset account...held...by a financial institution...for personal, family or household purposes").

OCT 16 2006

From: Michael Horgan [mikehorgan@msn.com]**Sent:** Wednesday, October 11, 2006 1:37 PM**To:** Rodger H. Rast**Subject:** Confirmation of Statement Made In Response Materials

After a substantial search of available information on the current law vs. proposed changes, I believe that the following supports my statement:

**3841. DEPOSIT INSURANCE COVERAGE; STORED VALUE CARDS AND OTHER
NONTRADITIONAL ACCESS MECHANISMS****Agency:**Federal Deposit Insurance Corporation (FDIC)**Priority:**

Substantive, Nonsignificant

Unfunded Mandates:

Undetermined

Legal Authority:12 USC 1813(l); 12 USC 1813(m); 12 USC 1817(l); 12 USC 1818(q); 12 USC 1819 (Tenth)**CFR Citation:** (To search for a specific CFR, visit the Code of Federal Regulations.)

12 CFR 330

Legal Deadline:

None

Abstract:

FDIC published a proposed regulation that would clarify the Insurance coverage of funds subject to transfer or withdrawal through the use of stored value cards and other nontraditional access mechanisms. This proposed rule is a revision of a proposed rule published by the FDIC in April of 2004 (the "First Proposed Rule"). See 69 FR 20558 (April 16, 2004). The purpose of the revised proposed rule (the "Second Proposed Rule") is to address certain issues raised by commenters in response to the original proposal.

Timetable: Action	Date	FR Cite
NPRM	04/16/04	69 FR 20588
NPRM Comment Period End	07/15/04	
Second NPRM	08/08/05	70 FR 45571
Second NPRM Comment Period End	11/07/05	
Final Action	10/00/06	

Regulatory Flexibility Analysis Required:

No

Small Entities Affected:

No

Government Levels Affected:

None

URL For More Information:<http://www.fdic.gov/regulations/laws/federal/propose.html>**Agency Contact:**

Christopher L. Hencke, Counsel, Legal Division, Federal Deposit Insurance Corporation,
Washington, DC 20429

Phone: 202 898-8839

RIN:

3064-AC80

July 8, 2005

MEMORANDUM TO: The Board of Directors

FROM: William F. Kroener, III General Counsel

Michael J. Zamorski Director

Division of Supervision and Consumer Protection

SUBJECT: New Proposed Rule on Insurance Coverage of Funds Underlying Stored Value Cards and Other Nontraditional Access Mechanisms**RECOMMENDATION:**

We recommend that the Board of Directors ("Board") seek comments on a new proposed rule that would clarify the insurance coverage of funds subject to transfer or withdrawal through the use of stored value cards and other nontraditional access mechanisms. This rule would replace the proposed rule published in April of 2004. See 69 FR 20558 (April 16, 2004). The new rule would provide: (1) that the funds underlying stored value cards (or other nontraditional access mechanisms) are "deposits" provided that the funds have been placed at an insured depository institution; and (2) that the insured owner of the "deposit" may or may not be the cardholder (depending upon the satisfaction of "pass-through" requirements). Also, through publication of the new rule, the FDIC would seek public comments on whether cardholders should receive mandatory disclosures about the insured status of the funds underlying their cards.

DISCUSSION:

For the FDIC, stored value cards (and other nontraditional access mechanisms) raise three primary issues. These issues are:

- Is there a "deposit"?
- If so, who is the insured owner?

- **Should cardholders receive disclosures about the insured status of the funds?**

These issues are important to the FDIC for obvious reasons. If a "deposit" exists, then the insured depository institution must report the deposit in its Call Reports. The deposit will be subject to assessments. The deposit will be insured (up to the \$100,000 limit). In the event of the failure of the depository institution, an identification of the owner of the deposit will be necessary in order for the FDIC to satisfy its obligation to pay insurance. Even in the absence of a bank failure, many cardholders will want to know whether they are protected by the FDIC.

Of course, the issues above are important to the FDIC only in those cases in which the stored value cards involve an insured depository institution. In the case of some stored value cards, no role is played by any insured depository institution. For example, in a "closed system," a cardholder will purchase his/her card directly from a merchant. The card will enable the cardholder — at a later point in time — to collect goods or services from the same merchant. In such a system, the merchant is not paid through a bank. Rather, the merchant is prepaid through the sale of the card. In the absence of the placement of funds at any insured depository institution, no insured "deposit" can exist. Such a system (not involving any insured depository institution) would not be governed by the FDIC's proposed regulation.

Below, the three primary issues are addressed with respect to systems involving insured depository institutions.

Is there a "deposit"?

"Deposit" is defined in the Federal Deposit Insurance Act ("FDI Act") at 12 U.S.C. § 1813(l). The information below is relevant in determining whether the term "deposit" applies to funds underlying stored value cards (or other nontraditional access mechanisms).

Funds underlying traditional access mechanisms. In the case of funds subject to transfer or withdrawal through traditional access mechanisms or payment instruments (such as checks, official checks, traveler's checks and money orders), the FDI Act sets forth a very simple rule: the funds are "deposits" provided that the funds have been placed at an insured depository institution. The only exceptions are certain narrow exceptions expressly created by Congress (such as an exception for bank obligations payable solely outside the United States). See 12 U.S.C. §§ 1813(l)(1), 1813(l)(4), 1813(l)(5).

General Counsel's Opinion No. 8. Though the definition of "deposit" in the FDI Act refers to traditional access mechanisms (such as checks), the definition does not mention "stored value cards" or other modern access mechanisms (such as computers). As a result, uncertainty has existed as to whether the term "deposit" applies to funds underlying these nontraditional access mechanisms. In 1996, the FDIC addressed the issue through General Counsel's Opinion No. 8 ("GC8"). See 61 FR 40490 (August 2, 1996). With respect to funds underlying stored value cards, the FDIC took the position — through GC8 — that the funds held by an insured depository institution are "deposits" if the institution maintains individual accounts for the various cardholders. At the same time, the FDIC took the position that the funds are not "deposits" if the institution maintains a pooled "reserve account" for all cardholders.

The First Proposed Rule. Following the publication of GC8, the industry developed new kinds of stored value card systems. These new systems prompted the FDIC, in April of 2004, to publish a proposed rule (the "First Proposed Rule"). See 69 FR 20558 (April 16, 2004). Through the First Proposed Rule, the FDIC sought to resolve questions that GC8 did not address. First, the FDIC recognized that many stored value cards do not involve a simple relationship between a depository institution and the cardholders. Rather, many stored value cards are issued by or through a third party or "sponsoring company." With respect to cards issued by a sponsoring company against an account at an insured depository institution, the FDIC proposed that the funds in such an account would be "deposits." Second, the FDIC recognized that some insured depository institutions have developed a system in which the institution maintains a pooled "reserve account" for all cardholders but simultaneously maintains individual accounts or subaccounts for the individual cardholders. The FDIC proposed that the funds in these subaccounts would be "deposits." Thus, under the First Proposed Rule, the only funds held by a bank that would not be "deposits" would be funds recorded in a pooled "reserve account" with no individual subaccounts.

The Second Proposed Rule. We are now recommending that the Board replace the First Proposed Rule with a new or "Second Proposed Rule." Under the new rule, all funds underlying stored value cards or other nontraditional access mechanisms would be "deposits" provided that the funds have been placed at an insured depository institution. The only possible exceptions would be the funds underlying cards with small balances (e.g., up to \$100) or funds placed directly

at an insured depository institution by anonymous cardholders. Although the Second Proposed Rule does not expressly include such exceptions, the FDIC would request comments as to whether such exceptions should be recognized. Otherwise, under the Second Proposed Rule, the FDIC's treatment of the funds underlying stored value cards and other nontraditional access mechanisms would be exactly the same as the FDIC's treatment of funds underlying traditional access mechanisms (such as checks or traveler's checks or money orders).

Unlike the First Proposed Rule, the new rule also would address a separate question: Assuming the existence of a "deposit," who is the insured owner? This question is discussed below.

Who is the insured owner?

Cardholders generally do not obtain stored value cards directly from an insured depository institution. Rather, they obtain the cards from a third party. For example, in the case of "payroll cards," employees will obtain their cards from the employer (or agent company on behalf of the employer). Similarly, in the case of "gift cards," the cardholders will purchase their cards from a retail store. The payroll card or the gift card will enable the holder to effect transfers of funds to merchants (through the merchant's point of sale terminal). Some cards will enable the holder to make withdrawals at automated teller machines ("ATMs"). Prior to the cardholders' use of the cards, the employer (in the case of payroll cards) or the retail store (in the case of gift cards) will place the necessary funds at an insured depository institution. Thus, the funds are placed at the bank by one party (the employer or retail store) for transfer or withdrawal by another party (the cardholder). This arrangement raises the following question: Who should be recognized as the insured owner of the deposit? The information below may be useful in resolving this question.

Checking accounts. In the case of a traditional checking account (including an employer's payroll checking account), the insured owner of the funds in the account is the accountholder. The FDIC does not provide insurance to the holders of outstanding checks.

Official checks. In the case of an official check issued by an insured depository institution, the insured owner is the payee because the check represents the institution's direct obligation to the payee.

Traveler's checks, money orders. In the case of a traveler's check or money order issued by an insured depository institution in exchange for cash, the insured owner is the payee. In the case of an instrument issued by a third party (such as an express company or money transmitter) against that party's account at an insured depository institution, the insured owner of the funds in the account is the third party and not the third party's payees.

Brokered deposits. In the case of funds placed at an insured depository institution by an agent or custodian, the FDIC provides "pass-through" insurance coverage. This means that the coverage "passes through" the agent or custodian to each of the actual owners. See 12 C.F.R. § 330.7(a). "Passthrough" coverage is not available, however, unless certain requirements are satisfied. First, the account records of the insured depository institution must indicate that the nominal accountholder is not the actual owner. See 12 C.F.R. § 330.5(b)(1). This requirement can be satisfied with an account title such as the following: "ABC Company as Custodian." Second, the identities and interests of the actual owners must be disclosed in records maintained by the depository institution or the agent or custodian or other party. See 12 C.F.R. § 330.5(b)(2). Third, the deposit actually must be owned by the alleged actual owner(s). See 12 C.F.R. § 330.3(h); 12 C.F.R. § 330.5(a)(1). For example, in the case of brokered deposits, the broker must relinquish ownership of the deposit to the broker's customers (e.g., by entering into an agency agreement with the customer). The broker cannot simply use the names of customers in order to obtain expanded insurance coverage for a corporate account.

The First Proposed Rule. The First Proposed Rule did not expressly discuss the FDIC's "pass-through" rules in connection with determining the owners of deposits underlying stored value cards or other nontraditional access mechanisms. Rather, the First Proposed Rule merely stated that the insurance coverage of any such deposits would be subject to the same rules that apply to any other deposits.

The Second Proposed Rule. The Second Proposed Rule would explicitly extend the FDIC's "pass-through" requirements to funds underlying stored value cards and other nontraditional access mechanisms. The rule could be summarized as follows:

- In the case of funds received by an insured depository institution from one party for transfer or withdrawal by the same party (e.g., funds placed into transaction accounts accessible solely by computer and not by checks), the funds would be insured to that party.
- In the case of funds received by an insured depository institution from one party for transfer or withdrawal by other parties (e.g., funds underlying payroll cards or gift cards), the funds would be insured to the first party unless (A) the bank's account records reflect the fact that the first party is not the actual owner; and (B) either the bank or the first party maintains records reflecting the identities of the persons holding the access mechanisms and the amount payable to each such person. If both of these requirements are satisfied, the funds would be insured to the persons holding the access mechanisms.

With respect to funds underlying payroll cards (but not gift cards), the FDIC would request comments on whether satisfaction of "pass-through" requirements should be mandated so that the funds held by an insured depository institution always would be insured to the employees (and not the employer). For example, a rule could be adopted under which insured depository institutions would be forbidden from accepting funds underlying payroll cards unless (1) the employer (or agent) maintains records reflecting the amount payable to each employee; and (2) the employer relinquishes ownership of the funds to the employees so that the employer cannot recover the funds in the bank under any circumstances (e.g., upon the expiration of a card).

Examples

The operation of the Second Proposed Rule can be illustrated through examples.

Example 1. A merchant sells gift cards directly to the public. The card may be used to collect goods or services from the same merchant. In this system (sometimes referred to as a "closed system"), the merchant does not receive payment through a depository institution but instead is prepaid through the sale of the card. No "deposit" exists in this system because no funds are placed at an insured depository institution.

Example 2. Same as above except that the merchant, following the sales of cards, places some or all of the collected money into an insured depository institution. The funds placed at the depository institution are "deposits." The insured owner of the deposits is the merchant and not the cardholders.

Example 3. An employer issues payroll cards in the total amount of \$250,000. In order to make payments on these cards, the employer places funds at an insured depository institution. The amount of funds placed at the bank, however, is only \$200,000. Moreover, the employer does not relinquish ownership and control of the funds. Rather, the employer retains the right to recover the funds if a card is not used within 30 days. In this scenario, a "deposit" exists at the insured depository institution in the amount of \$200,000. The insured owner of the deposit is the employer and not the employees.

Example 4. An employer issues payroll cards in the total amount of \$250,000. In order to make payments on these cards, the employer places \$250,000 at an insured depository institution. The funds are placed into individual accounts for the various cardholders; the employer does not retain the right to recover the funds. In this scenario, "deposits" exist in the total amount of \$250,000. The insured owners of the deposits are the employees.

Example 5. A retail store sells gift cards to the public in the total amount of \$500,000. These cards may be used to buy goods or services from any merchant that accepts major credit cards. In order to make payments on these cards, the retail store places \$500,000 into an account at an insured depository institution. The account is titled as follows: "Retail Store as Custodian for Cardholders." However, the retail store collects and maintains no information about the identities of the cardholders. In addition, the retail store retains the right to recover the funds underlying any expired cards. In this scenario, a "deposit" exists at the insured depository institution in the amount of \$500,000. The insured owner is the retail store and not the cardholders. Thus, the deposit is insured in the amount of \$100,000 (in aggregation with any other deposit accounts maintained by the retail store at the same insured depository institution) and uninsured in the amount of \$400,000.

Should cardholders receive disclosures?

The examples above reflect the fact that the insurability of funds underlying stored value cards and other nontraditional access mechanisms depends upon the circumstances. In some cases, no "deposit" will exist at an insured depository institution. In other cases, "deposits" may exist but the insured owners may not be the cardholders. In light of these various possibilities, cardholders may need to receive disclosures about the insured status of the underlying funds. We recommend that the Board seek comments on this issue.

CONCLUSION:

In response to the First Proposed Rule, the FDIC received comments from consumers as well as banks. Generally, consumers favored the proposed rule but banks opposed the rule. Banks feared that classification of funds as "deposits" would trigger various laws and regulations (such as the USA Patriot Act and Regulation E dealing with electronic fund transfers), with the result that costs would be increased and the development of stored value products would be stifled. We do not believe that the proposed rule would cause this effect because these other laws and regulations do not incorporate the definition of "deposit" in the FDI Act. We recommend that the Board authorize publication of the revised proposed rule (attached).

Staff member knowledgeable about this case:

Christopher Hencke Legal Division (X88839)

Attachment Concur:

Jodey C. Arrington Chief of Staff to the Chairman